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Can Uptick in Exports Bail Out Calif.'s Industrial Market?

A dramatic shift to export-related production has to occur for impact to be meaningful for region's logistics and warehouse base

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As the U.S. and California economies adjust to declining consumer spending and a weak dollar, some say exports could help divert the slumping economy toward growth.

Research has shown a direct correlation between imports and the demand for industrial space in Southern California. If outbound containers do increase at the Los Angeles and Long Beach ports, the natural question for commercial real estate is whether an uptick in exports can be meaningful enough to impact the Southern California industrial landscape.

"One long-term trend that may lead to more exports is the declining American dollar," said Thomas Galvin, a research analyst in the Ontario office of **Colliers International**.

"If the dollar continues to decline as many people believe, this will lead to a spur in exports. This is because goods produced here, in the U.S., will be comparatively cheaper versus foreign currencies."

The current monetary policy supporting a weak dollar, which translates to more exports, is what many are banking on for a recovery.

According to the University of California, Los Angeles' **Anderson Forecast** report for December, the national and state outlook calls for slow growth led by exports.

"The transition is being pushed along by the administration's weak dollar policy, which encourages exports and discourages the consumption of imports," wrote David Shulman, senior economist with the Anderson Forecast, in his report on the national economic outlook.

However, Shulman tempered that outlook and concluded that even an increase in exports would not be enough to "offset growth declines in consumer spending and state and local spending."

Exports for the nation are expected to increase 7.5 percent in 2010, according to the forecast.

At the state level, the outlook was very similar with growth not expected until the beginning of 2011 and the normal rate of growth to not resume until the middle of 2011.

"The keys to California's recovery remain, exports of manufactured and agricultural goods, a recovery in U.S. consumption which increases the demand for Asian imports and for products from California's factories, increased public works construction, and increased investment in business equipment and software," wrote Jerry Nickelsburg, senior economist with the Anderson Forecast, in his December outlook for the state.

October container traffic for the Los Angeles and Long Beach ports provided what some say is a sliver of hope.

In October, the Port of Los Angeles reported an 11.8 percent increase in exports from the year-ago period. Meanwhile, the Port of Long Beach continued to report declining exports with a 10.1 percent decline, albeit a smaller decline than what was reported earlier this year.

But it will not be easy for the Southern California region to turn its attention away from the handling of goods coming into the state to focus on production - if that happens at all. It would require a complete overhaul of the makeup of the region's industrial base.

SoCal Industrial Landscape

Even if exports tick up at the San Pedro Bay ports, Southern California's industrial landscape is dominated by warehouses and distribution centers, mainly used by third-party logistics providers or distributors involved in moving imports from the ports to a destination.

"Exports are not really a silver lining, since so much of our warehouse and distribution space in Southern California is geared to move things off boats [and] not readily onto them," Galvin said.

In the Inland Empire, in particular, Galvin said the region's industrial space was built to take imports, consolidate them and then move them to the rest of the country using trains or trucks.

"If that system was reversed, the Inland Empire could become a gathering point for manufactured and raw goods from the rest of the country," Galvin said. "Southern California remains the largest manufacturing base in the nation, and the Inland Empire would benefit if more of these manufactured goods were sent to consumers in Asia."

For Inland Empire industrial in general, Kurt Strasmann, managing director in **Voit Real Estate Services**' Anaheim office, said that in the last 60 days he has seen more activity. However, he could not peg those deals directly to export-related uses.

"The Inland Empire's got some tough times ahead, but I do think people are starting to make decisions and transaction volume is starting to increase," Strasmann said. "This is not the case in outlying areas, but it is the case in the western Inland Empire."
A groundbreaking was held Dec. 16 in Mira Loma for a 53,000-square-foot manufacturing and distribution center for Wakunaga of America Co. Ltd., a medicinal herbs provider.

Earlier in the year, the Riverside County Office of Foreign Trade helped facilitate a deal that brought South Korean auto manufacturer CT&T Motors to a site along Interstate 215 near Moreno Valley to build a manufacturing facility.

In Los Angeles County, KBL Group International, a sweater manufacturer, signed a 79,136-square-foot lease in November for manufacturing space in Santa Fe Springs.

Later that same month, the Downey City Council approved an agreement with **Industrial Realty Group**, which owns the site of what will be the future Tesla Motors manufacturing facility. Tesla will manufacture and assemble its Model S electric sedan at the new facility.

Despite recent activity, it is difficult to count whether more manufacturing deals will be enough to absorb the recent increase in vacant industrial space. The vacancy rate in the Inland Empire was 8.68 percent in third-quarter 2009, according to **CB Richard Ellis**. Los Angeles County had a 3.4 percent vacancy at the end of the third quarter, according to CB Richard Ellis.

Joseph Brady, president of Victorville-based **The Bradco Cos.**, said it is likely to take four years to absorb the inventory in the Inland Empire and Southern California.

"The challenge right now is market stability, and we think it's a couple years away," Brady said. "We have such a huge inventory in the Inland Empire that has to get absorbed. I think we have to wait for that to happen."

According to Lance Ryan, vice president of marketing and leasing in the Carson office of **Watson Land Co.**, most of the company's customers are involved in import-related activities.

"Of the over 10 million square feet of customers we have adjacent to the ports of Los Angeles/Long Beach, approximately 75 percent are involved in some form of distribution of product or third-party logistics," Ryan said. "This segment is almost exclusively import product, of which approximately 40 percent is consumed in the Southern California marketplace."

Ryan added that he is not aware of any export activity in the company's portfolio, which also includes Inland Empire properties.

Reality Check

Given the genetics of the region's industrial base, John Husing, vice president of Redlands-based Economics & Politics Inc., said significant expansion of exports could be an issue for a region mostly built out to handle imports.

"Exports are not a major factor in industrial space in Southern California," Husing said.

"Imports are much bigger and the problem we have is if the dollar strengthens, it will reduce imports but expand imports. It could work against the area unless - and that's a big issue - we start to see more production in Southern California."

Luciana Suran, an economist in the Boston office of **CBRE Econometrics Advisors**, added that any benefit from an increase in exports should be weighed against how much industrial space is available on the market.

"So much space was let up on the market that it's going to take a lot of manufacturing activity to get back to a place where we were before the recession started," Suran said. "A lot of factory space has been sitting there unused for the past year, year and a half. Once companies start producing, it's not that they're going to need new space because they already have plenty sitting there unused."

At the same time, should exports increase the activity will not go completely unnoticed in the industrial real estate market.

"It should help in the sense that it will keep things from getting worse," Suran said. "But, because exports tend to use warehouse space to a lesser extent than imports, it means recovery will be far off for California."

For the most part, if one looks at what is being moved out of the ports of Los Angeles and Long Beach, little of it is manufactured product.

Top exports at the Port of Long Beach, include petroleum coke, refined petroleum, waste paper, foods and chemicals. Top exports at the Port of Los Angeles last year included paper, scrap metal, fabrics, raw cotton and resins.

"By and large, the California ports, are more geared toward Asian imported goods," Suran said.

The transition from point A of being a goods-handling region to point B of being manufacturer is not a straight line.

"If you could be manufacturing and exporting, it would be wonderful," Husing said. "The problem you have with that is California has such a problem with its economy because of California law. Let's face it, California is repeatedly known as the place in the country that is the least competitive for production."

Husing also reiterated the amount of time necessary for such change to occur.
Meanwhile, the value of the dollar constantly changes, meaning growth based on exports could be just a fleeting hypothetical.

"For major effects to occur in the economy, there's a long adjustment necessary for that to occur, particularly if it means that suddenly we can produce when we don't currently have the facilities to produce," Husing said. "Maybe nationally the falling value of the dollar will have a positive effect. For Southern California, it's a different deal."

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